

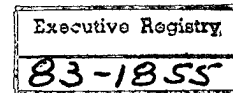


**THE SECRETARY OF COMMERCE**  
Washington, D.C. 20230

March 31, 1983

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MEMORANDUM FOR: Bill Casey

FROM: Mac Baldrige *Mac*  
SUBJECT: Economic Roundup

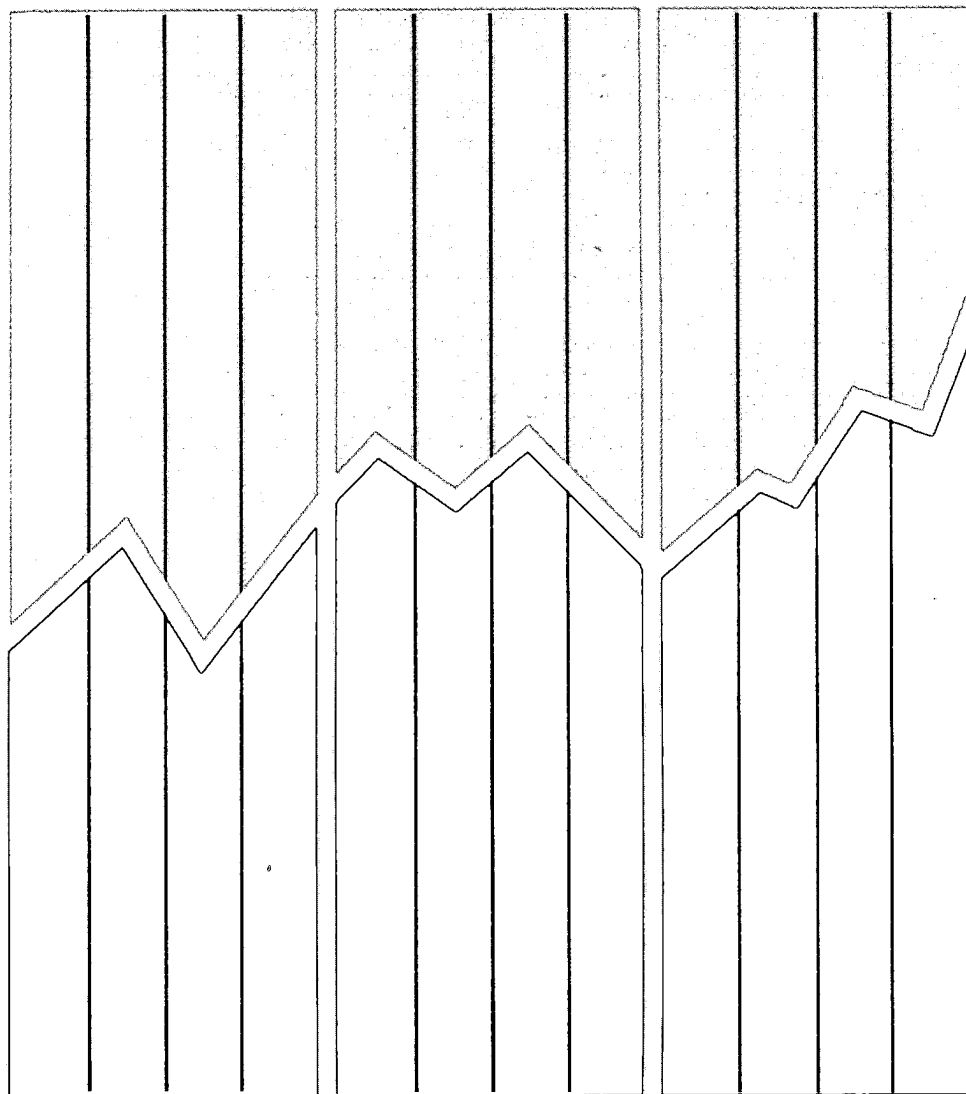
Enclosed is the March issue of our Monthly  
Economic Roundup.

Enclosure



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# The Economic Roundup



A MONTHLY REVIEW OF  
ECONOMIC DEVELOPMENTS



Office of Economic Affairs  
U.S. Department of Commerce

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THE ECONOMIC ROUNDUP

A Monthly Review of Economic Developments

Prepared by

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March 1983

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## SUMMARY

The principal questions about the economy center on the vigor and durability of the fledgling recovery. Following almost uniformly robust showings for January, February figures came in mixed. Weather conditions distorted the data for both months. Early readings for March continued mixed, but we need additional information on March and April before judging the strength of the recovery. Inflation has slowed to a standstill. The course of interest rates this spring will bear critically on the economic climate for the balance of the year.

- The Bureau of Economic Analysis projects that real GNP advanced at a 4-percent annual rate in the first quarter--the largest gain in two years. Strength was concentrated in homebuilding and domestic auto assemblies, as is typical in the early phase of recovery.
- In the months ahead, recovery should extend to stepped-up growth in consumer spending, outweighing sluggishness in business capital expenditures and net exports. Early signs of such a broadening of the advance have begun to surface.
- Tightening credit conditions remain the major risk to a sustained, vigorous expansion. Rising interest rates aborted the upturn following the 1980 recession and nipped a budding recovery in the spring of 1982. The possibility that interest rates may climb sharply again casts a shadow on what otherwise appears to be a conventional upturn in the making. A small rise in short-term interest rates during March suggests that the Fed is snuggling up credit conditions to slow the growth in money supply.
- Key measures of prices showed little net change over the past six months. The CPI posted rare declines in December and February. Plummeting petroleum product prices and stable food prices offset price advances elsewhere. As the favorable effects of food and energy developments dissipate, inflation measures should rise to about the 4 percent rate. A return to rapid inflation soon is very unlikely.

### HOUSING AND AUTOS LIFT GNP

Real GNP advanced at a 4-percent annual rate in the first quarter, according to a projection by the Bureau of Economic Analysis. This follows an upward revised 1.1-percent rate of decline in the previous period.

#### Residential Construction

Residential construction advanced vigorously for the second quarter in a row.

- The gains reflected the dramatic rise in housing starts since the summer of 1982. With starts at a 1.7 million unit annual rate in January and February, further increases in homebuilding outlays lie ahead.
- The easing of monetary policy last summer and the attendant lowering of interest rates were the major factors in the recovery of starts. Mortgage commitment rates fell from near 17 percent last June to under 13 percent recently, while deposit inflows to savings institutions increased markedly. New home sales surged 58 percent from last spring to early 1983. Anecdotal reports suggest that many first-time home buyers took advantage of more affordable monthly loan payments. With inventories of unsold houses at exceptionally low levels, the surge in sales generated a prompt production response.
- Though starts probably will retreat from the recent 1.7 million unit rate, and then show less spectacular gains, housing has fulfilled its customary role as a key leader in recovery.

#### New Car Assemblies

Domestic auto output accounted for another large portion of the projected first quarter increase in real GNP. After reducing assemblies to a 4.7-million unit annual rate in the fourth quarter in a successful effort to slash dealer inventories, manufacturers boosted production to about a 6-million unit annual rate in the first quarter.

- The first-quarter selling rate for domestic new cars averaged 6 million units, so dealer inventories were little changed. While overall stocks are in line with sales, supplies of smaller models are on the high side and larger model stocks are below average.

- Domestic new car sales also averaged 6 million units, at an annual rate, over the past seven months, compared with a total of 5-1/2 million units during the previous twelve months. The improvement has been more modest than the concurrent housing recovery would imply, even allowing for the lesser importance of interest rates in car buying decisions.
- Recent surveys indicate improved consumer attitudes toward car purchases. Additionally, domestic automakers are considering new promotions to replace the expired 11.9 percent financing offers.
- Domestic automakers currently plan to hold production in the second quarter at the first quarter level. Thus, auto output will not contribute to real GNP growth this spring.
- Very tentative plans for the third quarter suggest an assembly rate of 7 1/2 million units. These plans assume, though, that sales will break out of the doldrums in the next few months.

#### WEATHER COMPLICATES APPRAISAL OF RECOVERY'S VIGOR

Many economic series advanced robustly in January, then showed smaller gains or setbacks in February. Though the recovery has started, gauging its initial strength is difficult because of weather-related distortions in the data. After a mild December and a very mild January, the weather turned adverse in February, particularly during the week of the important labor market survey. Early readings for March also are mixed.

- The factory workweek in February dropped back to the December level, following a jump in January. A rebound in March would dispel worries about a faltering recovery. Data available so far for March include a slight decline in the purchasing agents composite index (albeit to a still favorable level), flat domestic new car sales, fewer auto assemblies, and a leveling off in weekly initial claims for unemployment benefits.
- Employment payrolls of nonfarm establishments fell 180,000 in February, after a 330,000 leap in January. Construction and retail trade accounted for most of the volatility. Other employment in the first two months of the year was modestly higher than in the last two months of 1982, as gains in durable goods manufacturing offset net job losses elsewhere.

- Though the estimation of industrial production draws heavily on the labor market report, the Fed discounted some of the setback in the average workweek in February. The 0.3 percent gain in industrial production in February marked the third successive rise. The recent advances have been split between products, chiefly automotive goods, and materials, following the inventory purge of late 1982.
- The composite index of coincident indicators edged down 0.2 percent in February, following a strong 1.1-percent gain in January. The January-February average stood 0.9 percent above the November-December average.
- Forward-looking indicators provide some reassurance that the recovery will proceed. The Composite Index of Leading Indicators rose 1.4 percent in February for its third very strong gain in a row. New orders for nondefense manufactured goods in January and February were 4 percent above the fourth quarter average. The low level of unfilled orders, however, may mean that industrial output will rise somewhat unevenly in response to incoming orders during the early phase of recovery.

#### BROADENING OF RECOVERY IN PROSPECT

Nonautomotive retail sales in February were 0.2 percent above January's level and 1.1 percent above the fourth quarter average. With vigorous discounting holding down prices, these gains mean solid advances in real terms. By February, the ratio of stocks to sales at nonauto retailers probably had returned to balance, i.e., near the 1977-81 average. The issue now is the strength of sales after the inventory clearance efforts have ended. Some promising signs for consumer spending have emerged.

- The average level of wage and salary income during the first two months of 1983 was 1.3 percent higher than in the fourth quarter. With inflation virtually nil over this period, this pick-up represents the strongest real advance in two years. The gain largely reflected the recovery in homebuilding and a rise in manufacturing payrolls.
- The increase in total personal income in early 1983 was less robust because farm subsidy payments dropped after a fourth quarter surge, unemployment benefit payments declined, and Social Security taxes rose.



- Consumer income will be boosted by higher income tax refunds in the second quarter. Through late March, refunds were running behind the year-ago pace, implying a good-sized catch-up in April and May. The third installment of tax rate reductions in July will also increase take-home pay, though interest and dividend withholding will temporarily offset roughly one-half of the projected \$36 billion, annual rate, infusion.
- Measures of consumer confidence have risen sharply. The University of Michigan's Consumer Sentiment Index reached 80.8 in March, its highest level since July 1978, while the Conference Board's Consumer Confidence Index climbed to 76.5, its highest mark since August 1981.
- Relative to consumer income, installment debt outstanding remains moderately low by past standards. In contrast with mortgages, delinquency rates on installment loans also continue at subdued levels.
- Finance rates on non-auto consumer loans have come down only slightly so far. The high yields should make aggressive lending by banks to consumers attractive once again, particularly in view of the recent large inflows of funds, sluggish short-term corporate borrowing, and lower yields on Treasury securities. Competitive pressures should bring consumer finance rates somewhat more in line with market rates.

Sustained growth in consumer purchases will spur broader increases in business output as inventory drawdowns end and as businesses shift toward rebuilding stocks. The easing of inventory liquidation in early 1983 mainly represented higher output in automotive and related industries and in building materials industries. Liquidation elsewhere apparently remained quite heavy.

- One sign of growing business confidence in the consumer outlook is the 8.4 percent jump in manufacturers' new orders for household durable goods between the fourth quarter and the January-February period.

Reduced business capital spending and sluggish net exports will tend to dampen near-term economic growth, as is typical at this juncture of a recovery.

- According to the survey conducted by the Bureau of Economic Analysis during late January and February, nonfarm businesses plan to reduce spending on plant and equipment by 3.8 percent in real terms this year. Further cutbacks are contemplated for the first half of this year, while a robust 4.6-percent snapback is planned for the second half.

- The current account balance dropped from a \$4.5-billion surplus in 1981 to a deficit of \$8.1 billion last year, largely because of an \$8.4-billion worsening in the merchandise trade deficit. A continuation of the 1982 second half performance, without much further deterioration, would result in a 1983 current account deficit of over \$20 billion.
- The merchandise trade deficit averaged \$3.7 billion per month during the November-February period, compared with an average deficit of \$4.7 billion over the prior four months. Lower oil imports more than accounted for the improvement. Reductions in nonoil imports, reflecting the inventory cutbacks, were offset by a drop in exports.
- Nonoil imports should grow with economic recovery. Exports probably will remain sluggish, given weakness among major trading partners, particularly LDC's, and the high level of the dollar.

#### INFLATION: DOWN, BUT NOT OUT

	<u>Annual Rate Percent Change for 6 Months Ended:</u>		
	<u>February 1983</u>	<u>August 1982</u>	<u>February 1982</u>
Consumer Price Indexes			
Total	0.4	6.6	5.3
Food and Beverages	1.1	3.2	4.1
Energy	-6.6	3.8	0.2
Other Items	1.9*	7.2	7.0
Producer Price Indexes			
Finished Goods	0.6	3.6	4.3
Intermediate Materials	0.1	-0.4	0.9
Crude Materials	-0.9	0.8	-8.9
Hourly Earnings Index	4.0	6.9	6.5

\*Probably an understatement because of the unduly large influence of falling mortgage rates in late 1982. A rental equivalence treatment of housing was introduced at the beginning of the year.

Increases in the CPI and PPI for finished goods came to a near halt over the past six months. Food costs advanced minimally, while petroleum prices plummeted. Gasoline prices in February were 16 percent below the March, 1981 peak. Prices of other items, on balance, rose moderately--roughly one-half the 10 percent pace of 1980.

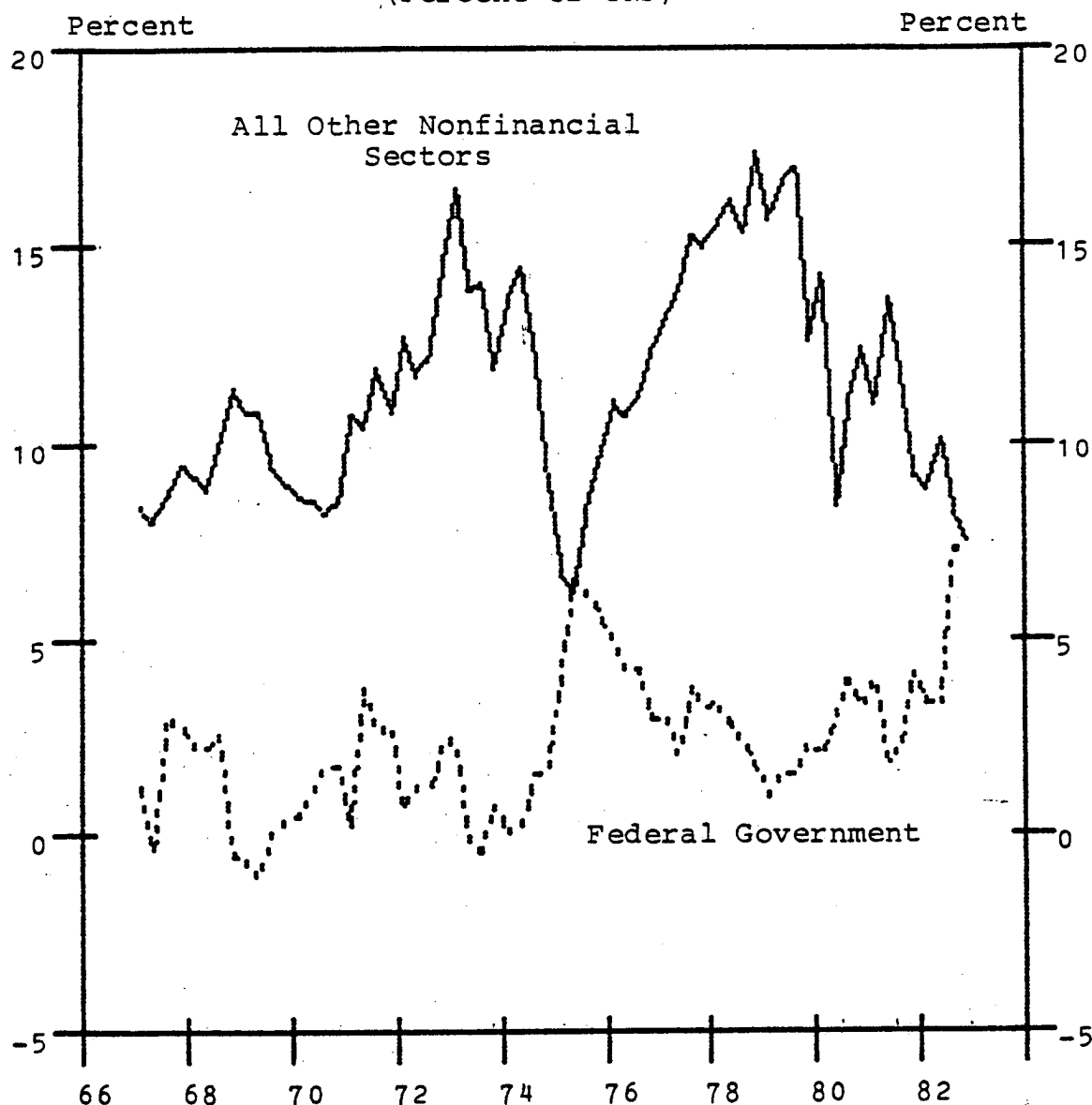
- Food prices appear ready to resume rising. Costs of pork and poultry advanced substantially at the retail level in February, but were offset by lower beef and produce prices. In the PPI, foodstuff prices at all three stages of processing showed the largest increases in February since the spring of last year. The payment-in-kind subsidy program for farmers has generated larger than expected declines in planned crop plantings for this year (corn down 33 percent, wheat down 18 percent, soybeans down 8 percent, and cotton down 23 percent).
- The recent OPEC agreement, if it holds, may stabilize crude oil prices in world markets. If so, much of the decline in crude oil prices already has passed through to consumers. The five cent per gallon increase in the Federal tax on gasoline takes effect on April 1st.
- Wage rate increases continue to trend down. With productivity improving, the climb in unit labor costs this year should be quite modest. While inflation may pick up to about a 4-percent rate, a return to rapid inflation any time soon is very unlikely.

#### MONEY AND CREDIT CONDITIONS: KEY TO SUSTAINED RECOVERY

During the second half of last year, funds raised in the credit markets by nonfinancial sectors represented a moderate 15 percent of GNP. The Federal Government accounted for close to one-half of the borrowing, reflecting the large budget deficits and reduced private credit demands. With stronger private credit demands in prospect, interest rates may rise unless the Fed accommodates faster credit growth.

- As the chart below indicates, Federal government borrowing usually declines as private credit demands expand. Despite the offset, total borrowing usually rises relative to GNP during recoveries. In the coming year, the government's need for funds will be higher than usual, leaving less for the private sector as a share of the total that will be permitted by the Fed.
- Private credit demands are already strengthening. Consumer installment credit grew more rapidly over the three months ended in January, and should continue to grow along with consumer spending. Home mortgage lending rose in late 1982, and mortgage commitments advanced substantially in the first two months of this year. While corporate borrowing is muted by inventory liquidation and reduced capital spending, it will accelerate again as the recovery proceeds.

# Increases in Debt Outstanding (Percent of GNP)



## Selected Interest Rates (Percent)

<u>Week Ended</u>	<u>Federal Funds</u>	<u>Bank Prime</u>	<u>6-month T-bill</u>	<u>AAA Corporate Bond</u>	<u>Mortgage Commitment</u>
1982					
Mar 26	14.48	16.5	12.7	14.5	17.0
Jun 25	14.17	16.5	13.0	15.1	16.7
Sep 24	10.31	13.5	9.4	12.8	15.2
Dec 31	8.79	11.5	8.1	11.8	13.6
1983					
Jan 28	8.44	11.0	8.1	11.9	13.1
Feb 25	8.47	11.0	8.0	11.8	13.0
Mar 25	8.75	10.5	8.5	11.8	12.9

- The Federal Funds rate rose to 8-3/4 percent in the week ended March 23, and has remained elevated. Over the previous ten weeks, this key interest rate fluctuated narrowly between 8.4 and 8.6 percent--the steadiest performance since the formal adoption of monetary targeting on October 6, 1979. The yield on new six-month Treasury bills climbed from 7.9 percent in early March to 8.7 percent at the latest auction. The interest rate increases coincided with heavier government borrowing late in the quarter. In the second quarter, the Federal Government is expected to borrow \$40-45 billion.
- The narrow money supply, M1, grew at a 12.7 percent annual rate over the eight months ended in February. M2, over the same period, grew at a 15.2 percent annual rate. Both measures are above the targets indicated in mid-February by the Fed. The fastest growing component of M2 has been the Money Market Deposit Accounts. Introduced in mid-December, they have attracted assets from money market funds, large denomination CD's (a component of M3), savings accounts, and small time deposits.

ECONOMIC INDICATORS

	<u>Feb</u>	<u>Jan</u>	<u>Dec</u>	<u>Nov</u>	<u>Oct</u>	<u>Sept</u>
<u>General Indicators</u> (% change)						
Composite Index of Leading Indicators*	1.4	3.5	1.1	0.3	0.8	1.2
Composite Index of Coincident Indicators*	-0.2	1.1	-0.2	0.1	-1.6	-0.7
Composite Index of Lagging Indicators*	-0.6	-1.0	-1.4	-2.0	-0.6	-0.7
NAPM Composite Diffusion Index (percent)	56.6	45.7	41.0	37.3	37.7	37.7
<u>Employment</u>						
Total Employment (change in 000's)	-43	12	-38	-48	-369	-159
Payroll Employment (change in 000's)	-180	330	-215	-127	-387	-48
Unemployment (change in 000's)	44	-590	130	330	261	384
Unemployment Rate (percent)	10.2	10.2	10.7	10.6	10.3	10.1
Initial Claims for Unemployment Insurance (000's)	478	507	531	616	651	653
Factory Workweek (hours)	38.9	39.8	38.9	38.9	38.8	38.8
<u>Production and Orders</u>						
Industrial Production (% change)	0.3	1.3	0.2	-0.6	-1.2	-0.8
Capacity Utilization, Manufacturing (%)	68.5	68.3	67.5	67.4	68.0	69.2
Auto Production (mil. units, AR)	6.4	5.9	5.4	4.4	4.3	4.9
Total New Orders (% change)	-2.2	2.5	3.9	0.4	-4.1	1.2
Nondurable Goods (% change)	-1.1	-0.5	-0.1	-0.4	-3.4	1.8
Durable Goods (% change)	-3.2	5.7	8.5	1.4	-5.0	0.4
Nondefense Capital Goods (% change)	-7.2	1.5	-0.1	0.0	-0.4	7.3
<u>Inventories</u>						
<u>Manufacturing and Trade</u>						
Inventories (percent change)		-0.6	-0.9	-1.1	-0.2	0.2
Inventory/Sales Ratio		1.47	1.51	1.52	1.55	1.52
Chg. in Auto Inventories (mil. units, AR)	0.5	0.3	-0.4	-2.2	-0.8	-0.6
<u>Prices and Wages</u>						
Consumer Price Index (% change)	-0.2*	0.2*	-0.3	0.0	0.4	0.1
Food (% change)	0.0*	0.1*	0.0	0.0	0.2	0.2
Energy (% change)	-3.7*	-2.5*	0.3	0.8	1.3	-0.5
All Other Items (% change)	0.4*	0.5*	-0.2	-0.1	0.2	0.1
<u>Producer Prices</u>						
Finished Goods (% change)	0.1	-1.0	0.2	0.6	0.4	0.1
Intermediate Goods (% change)	-0.1	-0.3	0.0	0.3	0.0	0.2
Crude Goods (% change)	0.6	-0.3	-0.3	1.0	-0.3	-1.2
Hourly Earnings Index (% change)	0.1	0.4	0.6	0.3	0.5	0.1
Hourly Earnings Index (12-month % change)	5.5	5.4	6.0	5.6	6.3	6.1

\* - revised methodology

ECONOMIC INDICATORS (cont'd)

	<u>Feb</u>	<u>Jan</u>	<u>Dec</u>	<u>Nov</u>	<u>Oct</u>	<u>Sept</u>
<u>Consumer Spending and Income</u>						
Personal Income (% change)	0.1	0.2	0.3	0.7	0.5	0.2
Wages and Salaries (% change)	-0.1	1.0	0.5	0.0	0.1	0.0
Disposable Personal Income (% change)	0.0	0.3	0.2	0.8	0.4	0.3
Real Disposable Personal Income (% change)		0.0	0.1	0.7	-0.2	-0.2
Personal Consumption Expenditures (% change)	0.0	0.6	0.3	1.0	0.6	1.1
Real Personal Consumption Expenditures (% change)		0.3	0.2	1.0	0.0	0.6
Retail Sales (% change)	-0.4	-0.4	0.0	1.7	1.1	0.9
Domestic New Car Sales (mil. of units, AR)	6.0	6.0	6.1	6.8	5.5	6.0
Saving Rate (percent)	5.6	5.6	5.9	6.0	6.2	6.3
Consumer Installment Credit (change, \$ millions)		2929	2418	2015	-131	1256
Consumer Confidence Index (Conf. Board)	65.8	58.0	53.5	54.8	49.7	54.4
Consumer Buying Plans (Conf. Board)	75.8	71.9	75.2	80.5	66.7	75.3
Consumer Sentiment (U. Mich.)	74.6	70.4	71.9	72.1	73.4	69.3
<u>Construction</u>						
Real Construction Expenditures (% change)		6.8	-1.9	1.4	-0.1	-0.2
Private Residential (% change)		6.3	3.9	4.7	3.1	-1.3
Private Non-residential (% change)		3.8	-2.4	-0.4	-1.7	0.7
Public		14.1	-9.5	0.3	-0.3	-0.9
New Home Sales (% change)	-5.9	12.7	-3.5	13.3	1.7	21.6
Housing Starts (000's of units, AR)	1756	1707	1280	1361	1142	1134
Housing Starts (% change)	2.9	33.4	-6.0	19.2	0.7	8.4
Housing Permits (% change)	1.0	13.3	9.4	1.7	16.8	13.0
Mortgage Interest Rates, FHLMC (percent)	13.04	13.31	13.62	13.83	14.61	15.43
<u>Money and Credit Conditions</u>						
M1 (% change)	1.8	0.8	0.9	1.1	1.2	1.1
M2 (% change)	2.0	2.5	0.7	0.8	0.7	0.7
Federal Funds Rate (percent)	8.51	8.68	8.95	9.20	9.71	10.31
3-month Treasury Bills (percent)	8.13	7.81	8.01	8.04	7.75	8.20
Bank Prime Rate (percent)	10.98	11.16	11.50	11.85	12.52	13.50
Treasury Bond Yields (percent)	10.60	10.37	10.33	10.18	10.51	11.48
Corporate Bond Yields (percent)	12.11	12.04	12.15	11.89	12.63	13.78
Commercial and Industrial Short Term Credit (% change)	-0.7	1.3	-1.8	-2.3	0.2	0.6

ECONOMIC INDICATORS (cont'd)

	<u>Feb</u>	<u>Jan</u>	<u>Dec</u>	<u>Nov</u>	<u>Oct</u>	<u>Sept</u>	<u>Aug</u>
<u>International Trade</u>							
Merchandise Exports (\$ billions)	16.3	17.4	16.3	15.8	16.7	17.3	17.5
Merchandise Imports (\$ billions)	19.9	21.0	20.0	19.7	21.9	21.5	24.0
Trade Balance, c.i.f. (\$ billions)	-3.6	-3.6	-3.7	-3.9	-5.3	-4.2	-6.5
<u>National Accounts</u>							
	<u>1982</u>				<u>1981</u>		
	<u>IV</u>	<u>III</u>	<u>II</u>	<u>I</u>	<u>IV</u>	<u>III</u>	<u>II</u>
Nominal GNP (% change, AR)	2.6	5.8	6.8	-1.0	3.0	11.4	5.3
Real GNP (% change, AR)	-1.1	0.7	2.1	-5.1	-5.3	2.2	-1.5
Real Disposable Income (% Change, AR)	0.3	1.3	3.1	-1.9	1.2	4.8	0.6
Real Consumption (% change, AR)	4.5	0.6	2.5	2.5	-3.3	2.9	-2.7
Real Nonresidential Fixed Investment (% change, AR)	-6.0	-7.6	-11.8	-5.0	0.6	9.3	1.1
Real Residential Fixed Investment (% change, AR)	39.3	-5.3	12.9	-10.2	-25.3	-31.9	-17.4
Housing Starts (000's of units, AR)	1261	1122	950	903	870	961	1176
Change in Business Inventories (\$72, billions)	-20.3	3.4	-4.4	-15.4	4.8	16.5	12.1
Net Exports (\$72, billions)	27.2	27.5	35.7	36.9	36.5	39.2	44.2
Real Government Purchases (% change, AR)	12.0	8.4	-5.3	-2.9	7.0	3.6	-4.1
Fixed-weighted Price Index (% change, AR)	4.9	5.9	4.1	4.8	8.5	8.9	8.4
<u>Corporate Profits (% change)</u>							
Before-tax (current production)	0.8	6.9	-1.1	-14.6	-4.8	4.3	-7.6
After-tax (current production)	2.7	5.3	-0.4	-10.6	1.4	4.5	-2.8
Before-tax (book)	-0.8	5.0	0.0	-20.7	-7.2	3.5	-10.9
After-tax (book)	0.0	2.7	1.1	-20.6	-3.9	3.1	-9.5

3/31/83